Report of the Tennessee Advisory Commission on Intergovernmental Relations

Insurance as an Alternative to Surety Bonds for Public Officials

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Alternatives to Surety Bonds for Public Officials

Good government depends on able, loyal, and dedicated public officials. Particularly for those officials who handle large amounts of money or have duties that, if not properly performed, could lead to financial loss for the government, safeguards are necessary to protect the public interest. To guard against the risk that public officials will not faithfully perform their duties and thereby protect public funds, governments have long required individual surety bonds—contracts in which a surety guarantees the governmental entity that the office holder will successfully perform his or her duties.

Individual surety bonds have been required in Tennessee since the 19th century to protect against losses caused when public officials do not faithfully perform their official duties. These bonds are intended to protect the public and compensate those suffering loss or injury by reason of misconduct or neglect in office.[1] These bonds do more than cover losses; they also encourage officials to perform the duties of office by holding them personally liable, giving them "skin in the game", for any claims that are made against the bond. Sureties will require the public official to reimburse them the amount paid on the claim. The amount of the bond depends on the office and in some cases the amount of money handled by the office. Bond amounts range from $2,000 for county surveyors to well over $10 million for county trustees in Shelby and Davidson counties.

Tennessee law requires various local officials, mostly those serving county governments, to execute individual surety bonds as a prerequisite to taking office. The laws requiring these bonds appear in several parts of state law, covering 29 different offices of local government.[2] No state offices require individual surety bonds, although blanket coverage in the form of insurance is required for state officials and employees.[3] County governments are also required to provide blanket coverage for all employees not covered by individual surety bonds.[4] City governments are not.

Senate Bill 624 by Senator Norris [House Bill 1004 (Todd)], which was sent to the Commission by the Senate State and Local Government Committee, proposed changing current law to allow insurance as an alternative to individual surety bonds.[5] The bill would allow a governmental entity to buy a policy or cover the same risk by participating in an insurance pool.[6] The bill allows any one of three options: (1) government crime coverage, (2) employee dishonesty insurance, or (3) equivalent coverage that insures the faithful performance by officials and their employees of their fiduciary duties and responsibilities. The bill sets the

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[1] Holben et al. 2012.

[2] Titles 5, 6, 7, 8, 9, 13, 18, 49, 54, and 67 of the Tennessee Code Annotated each contain surety bond requirements for public officials.

[3] Tennessee Code Annotated, Section 4-4-108.

[4] Tennessee Code Annotated, Section 8-19-101. See appendix B

[5] See appendix A.

[6] The bill refers to pools established pursuant to Tennessee Code Annotated, Section 29-20-401.

minimum amount of coverage at $400,000 per occurrence. According to the legislature's Fiscal Review Office, the bill could increase local governments' tort liability, which could increase their expenditure if the number of lawsuits increased. However, the cost of insurance should be less than the cost of surety bonds, but the likely difference is impossible to determine because the coverage limits and deductibles are unknown.

It is unclear whether an insurance policy can be written that provides the same coverage as Tennessee's public official surety bonds. However, even if such a policy could be written and found in the marketplace, it is widely believed that it would be prohibitively expensive. While other states allow insurance instead of surety bonds, no state requires the insurance to be the equivalent of Tennessee's surety bonds.[7] If it did everything a surety bond did and was available at the same cost, it would essentially be a surety bond. In that case, there seems to be little advantage in providing insurance as an alternative.

The consensus of the Commission is that Senate Bill 624 is not needed, at least not in its current form. It is not clear that it would provide the same safeguards as Tennessee's individual surety bond requirements, particularly as they relate to holding individual office-holders accountable. The Commission would, however, endorse a provision allowing blanket coverage that is the equivalent of the individual surety bonds currently required, which could be less expensive and easier to administer. For example, the State of Virginia buys a bond that covers multiple officers, is conditioned on faithful performance of their duties, and holds them individually accountable by allowing the company selling the bond to recover any claim paid to the state because of the failure of any office holder to faithfully perform his or her duties.[8] Georgia authorizes county governments to purchase similar bonds. Appendix H includes an example of how this might be done.

[7] See appendix D.
[8] See appendix E.

A Key Difference between Surety Bonds and Insurance—Personal Accountability

The choice among risk management tools can be seen as a decision about who will be liable for losses resulting from the actions of public officials, the official or the taxpayer. Surety bonds make the public official personally liable for losses. The various forms of insurance do not. A public official surety bond is a contract between three parties in which one party (the surety, a bond or insurance company) guarantees a second party (the obligee, a city or county) that a third party (the principal, a public official) will successfully perform his or her legal obligations. These bonds hold the principal personally liable for not faithfully performing the duties of office. There are two main types of public official surety bonds, individual surety bonds and blanket surety bonds. As the names suggest, individual surety bonds provide coverage for a single officer, while blanket surety bonds cover a group of officers. With both types, the official owes a duty of indemnification to the surety if the surety makes payment under the bond.

Most states require individual surety bonds for their county officials, and several allow for some form of blanket bond coverage in place of individual bond requirements. States' laws rarely define the term "blanket surety bond" or "blanket bond," and the phrase "blanket bond" is sometimes confusingly used to refer to a two-party contract that does not create an obligation on the part of the principal. When used in this manner, the contract is not a surety bond; it is insurance.

A handful of states allow for some form of insurance to be used in place of an official bond requirement. Insurance transfers the risk of loss from one party (e.g., a city or county) to another (e.g., an insurance company) in exchange for payment (premium). Insurance itself does not hold the official personally liable but transfers liability to the insurance company or insurance pool and, if the specific act is not covered, ultimately the taxpayer. Further, with insurance, taxpayers cover the cost of deductibles as well as premium payments. While surety bonds hold public officials personally responsible, and therefore provide an incentive to properly perform the duties of office, insurance policies do not.

Individual Surety Bonds—Current Statutory Requirements

Tennessee's statutes requiring public official bonds give guidance on

- the officials required to give bond,
- the coverage and amount of the bond,
- the process for approval of the bonds, including the approving authority,
- the financial responsibility for paying the cost of the bonds, and
- the consequences of not providing a required bond.

Various local officials, mostly those serving county governments, are required to execute individual surety bonds as a prerequisite to taking office. The laws requiring these bonds appear in several parts of state law and cover 29 different offices of local government, including city managers, as well as city employees who handle money. With modified city-manager-council charters, the city council determines which employees must give a bond. Bond amounts for city employees are set locally. No state offices require individual surety

bonds, although blanket coverage in the form of insurance is required for state officials and employees. County governments are also required to provide blanket coverage for all employees not covered by individual surety bonds. City governments are not.

In Tennessee, the surety bond process is regulated at every step. Title 8, Chapter 19 "Bond of Officers," provides the general bond requirements, procedures, and authority for the issuance of the bonds. The requirements for specific officials and the sureties on their bonds are also controlled by statutory language. Tennessee law requires the Comptroller of the Treasury to prescribe forms for all bonds, subject to the approval of the Attorney General and Reporter.[9] Tennessee also requires that the governmental entity pay for the bond, but also provides[10] in the alternative that the official may deposit cash equal to the amount of the bond in place of a surety bond.[11] City charters often have additional surety bond requirements for certain officers and employees who handle money. The charters also usually require the bond amounts to be set by a municipal legislative body or board. Surety bonds are typically sold by insurance companies, which are regulated by the Department of Commerce and Insurance.

Tennessee Code Annotated, Section 8-19-106, provides that "the respective counties shall pay the premiums for such bonds and the registration fees." Statutes also generally require that the official must be bonded before taking office. For example, the statute for the county trustee states in part that "the county trustee may enter upon the discharge of the duties of office, after first giving bond, and an oath for the faithful performance of the duties of the office."[12] If the bond is not executed within the prescribed time, the individual must vacate the office.[13]

Amount of Bond

Tennessee statutes requiring individual surety bonds for public officials generally set minimum bond amounts. See table 1. The statutes make clear that local governments can require higher bond amounts. Public Chapter 315, Acts of 2013, increased the bond amounts for many officials. Bond amounts that are not set in statute may be determined in one of several different ways: based on revenue or population; or as determined by a court, county legislative body, or judge. Minimum bond amounts for certain positions that handle large sums of money are based on revenue. For example, a county trustee's minimum bond amount "shall be based on the revenues as follows: (1) Four percent (4%) up to three million dollars ($3,000,000) of the funds collected by the office; (2) Two percent (2%) of the excess over three million dollars ($3,000,000) shall be added; and (3) The amounts indicated in subdivision (b)(1)-(2) shall be cumulative." The bond amounts for some county trustees are several million dollars.

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[9] Tennessee Code Annotated, Section 8-19-101(b)(1).
[10] Tennessee Code Annotated, Section 8-19-106.
[11] Tennessee Code Annotated, Section 8-19-120.
[12] Tennessee Code Annotated, Section 8-11-102.
[13] Tennessee Code Annotated, Section 8-19-117.

Table 1. Public Officials and Their Bond Amounts

Office/Agency	TCA Reference	Amount of Bond	Elect/Appoint
Assessor of Property	67-1-502 and 505	$50,000	Elected. 4 years
Chancery Court Clerk and Master	18-2-201 through 213 and 18-5-101	$50,000-$100,000 Population based	Appointed. 6 years
Circuit/Criminal/Special/ General Sessions Clerk	18-2-201 through 213 and 18-4-101	$50,000-$100,000 Population based	Elected. 4 years
Commissioner/Receiver	18-2-201 through 213	Court determined	Court determined
Constable	8-10-101 and 106	$4,000 to $8,000 County discretion	Elected. 2 to 4 years
Coroner	8-9-101 and 103	$2,500	Elected by County Board. 2 years
County Clerk	18-2-201 through 213 and 18-6-101 through 115	$50,000-$100,000 Population based	Elected. 4 years
County Engineer	54-9-131 and 132	$10,000	Employed by Road Commission.
County Executive/Mayor	5-6-101 and 109	$100,000	Elected. 4 years
County Road Commission	54-9-116 and 119	Set by County Board	Elected. 1, 2, or 3 years
County Highway/Bridge Funds	54-4-103 (c)	$100,000 or greater	
County Highway Superintendent/Chief Administrative Officer	54-7-105 and 108	$100,000	Elected. 4 years
Development District	13-14-114	Revenue-based Calculation Formula	4 years. Some statutorily required. Some appointed by Senators.
Director of Accounts and Budgets (1957 Act)	5-13-103	$100,000 or greater	Appointed by County Mayor
Director of Finance (1981 Act)	5-21-106 and 109	$100,000 or greater	Appointed by Financial Management Committee

Office/Agency	TCA Reference	Amount of Bond	Elect/Appoint
E911 District	7-86-119	Revenue-based Calculation Formula	Appointment varies based on population size.
Human Resource Agency	13-26-110	Revenue-based Calculation Formula	4 years. Some statutorily required. Some appointed by Senators.
Public School Fiscal Agent	49-3-315(b)(3)	Revenue-based Calculation Formula	
Notary Public	8-16-101 through 104	$10,000	Elected by County Board. 4 years
Process Server	8-8-108	$5,000 (Shelby $15,000)	Judicial Appointment
Purchasing Agent	5-14-103(c)	$100,000 or greater	Appointed by County Mayor
Register of Deeds	8-13-101 through 103	$50,000-$100,000 Population based	Elected. 4 years
Sheriff	8-8-103	$100,000 or greater	Elected. 4 years
Special Deputy	8-8-303	$50,000	Appointed by Sheriff
Director of Schools	49-2-301 and 9-3-301(c) and 49-2-102	$50,000 or greater	Appointed by Board of Education
Surveyor	8-12-101 and 102	$2,000	Elected by County Board. 4 years
Trustee	8-11-101 through 103	Revenue-based Calculation Formula	Elected. 4 years
City Manager (and employees dealing with funds)	6-21-104 and 105	Set by ordinance of board of commissioners, except where the amount is prescribed in charter.	Appointed by Board of Commissioners

Office/Agency	TCA Reference	Amount of Bond	Elect/Appoint
All city officers/employees dealing with funds (Modified City Manager-Council Charter)	6-35-411	Council sets the bond amount and determines who must have one.	

Source: Tennessee Code Annotated and Tennessee Comptroller of the Treasury

Cost

The price of an individual surety bond depends on the bond amount required, the obligations the bond covers, and the background of the individual being bonded. Background checks include credit checks, criminal background checks, and a review of prior bonding history. The higher the bond amount, the higher the price for that bond. For example, Williamson County recently paid $113 per year for the county clerk's $50,000 bond and $6,000 per year for the county trustee's near $10 million bond.[14]

Coverage

Understanding what a public official surety bond covers in Tennessee requires analyzing (1) the bond, (2) the statute requiring the bond, (3) any statutes governing the conduct of the bonded official, and (4) applicable case law.[15] The Comptroller of the Treasury's website provides the standard public official bond form, which includes the terms of the bond required by Tennessee law.[16] The legislature provided the exact language that the surety bond must include:

> In every case, provisions of this code to the contrary notwithstanding, the official bond of every county public official shall be conditioned as follows and not otherwise:
>
> That if the _____________(Principal) shall:
>
> 1. Faithfully perform the duties of the Office of ____________County during such person's term of office or continuance therein; and
> 2. Pay over to the persons authorized by law to receive them, all moneys, properties, or things of value that may come into such principal's hands during such principal's term of office or continuance therein without fraud or delay, and shall faithfully and safely keep all records required in such principal's official capacity, and at the expiration of the term, or in case of resignation or removal from office, shall turn over to the successor all records and property which have come into such principal's hands, then this

[14] Email from Wayne Franklin, October 15, 2013.
[15] Shreves and Coffee 1997.
[16] See appendix C.

> obligation shall be null and void; otherwise to remain in full force and effect.[17]

The first and most significant obligation in the bond is for the principal to "faithfully perform the duties of the office." Faithful performance of duties means fulfilling them without dishonesty, malfeasance, or negligence, and without damage to the governmental entity or the public, whether intentionally or negligently.[18] The duties are the key. The duties are what the law defines them to be.[19] Part 2 of the bond form, above, lists the broad duties that the official must perform. The statute establishing that general surety bond requirement also says that the duties that must be faithfully performed include the duties specified in the statutes that establish the specific offices.[20] For example, Tennessee Code Annotated, Section 8-11-104, lists several specific duties for county trustees. Other officials have similar statutes detailing the duties of office. Tennessee has a statute that broadly outlines the obligations covered by required official bonds at Section 8-19-301:

> Every official bond executed under this code is obligatory on the principal and sureties thereon: (1) For any breach of the condition during the time the officer continues in office or in the discharge of any of the duties of such office; (2) For the faithful discharge of the duties which may be required of such officer by any law passed subsequently to the execution of the bond, although no such condition is expressed therein; (3) For the use and benefit of every person who is injured, as well by any wrongful act committed under color of such officer's office as by the failure to perform, or the improper or neglectful performance, of the duties imposed by law.

Some officials also have specific statutes addressing the scope of liability on the bonds, such as the county clerk: "the official bonds of clerks, executed under this code, are obligatory on the principal and sureties for every wrongful act or failure of duty in the clerk's official capacity, whether embraced in the condition of the bond or not, or growing out of a law passed subsequently to its execution."[21]

Claims against Surety Bonds

Typically, the governmental entity, such as the county, is the party that would file a claim against the public official's surety bond if there were a loss. However, Tennessee law provides that the public can make claims against the bond.[22] Under an insurance policy, unless the policy specifically allows third-party recoveries, only the insured will be able to recover for a loss. Surety bond claims are rare and unexpected because of the screening process required.

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[17] Tennessee Code Annotated, Section 8-19-111(b).
[18] Price, McDonnell, and Howald 2006.
[19] Ibid.
[20] Tennessee Code Annotated, Section 8-19-111(c)
[21] Tennessee Code Annotated, Section 18-2-206.
[22] Tennessee Code Annotated, Section 8-19-301 states that it is "for the use and benefit of every person who is injured."

To have a claim against a bond, the governmental entity must show a loss. When a claim is made, the surety company investigates and, if it is a valid claim, will pay and then turn to the official for reimbursement.

Blanket Surety Bonds

Blanket surety bonds establish a three-party relationship with personal liability remaining with the official for any claims against the bond. Unfortunately, confusion is often created because the phrase "blanket bond" is sometimes used to refer to a two-party insurance contract, which does not create an obligation on the part of the official. For example, Tennessee Code Annotated, Section 4-4-108, requires a "blanket surety bond" to cover certain state-level officers and employees, but an insurance policy is used.

Twenty-three states allow some form of blanket coverage instead of individual surety bonds. Two states, New Hampshire and Virginia, require only blanket coverage.[23] Of these, only Virginia and Georgia appear to require surety bonds. Virginia buys a blanket surety bond that covers multiple state and local officers, conditioned on faithful performance of their duties, and holds them individually accountable by allowing the company selling the bond to recover any claim paid to the state because of the failure of any office holder to faithfully perform his or her duties. A list of the positions covered, along with the dollar amounts of coverage for each position, is attached to the bond and submitted to the surety company. Their 2013-2014 blanket surety bond totals $203,480,818 and covers approximately 1,119 state officials and local constitutional officers for an annual premium of $467,976. The dollar amount of coverage for the positions ranges from $3,000 to $3 million.[24]

Several counties in Georgia have taken advantage of the opportunity to use blanket surety bonds to meet their individual surety bond requirements. The risk management director of Augusta-Richmond County, Georgia, explained that the county uses a blanket surety bond to cover all officials with bond amounts of $25,000 or less and buys individual surety bonds for those officials with bond amounts over $25,000. This is required by the particular surety company the county uses and not because of state law. Before using the blanket surety bond, Augusta-Richmond County spent $6,250 on individual bonds for those positions with bond amounts of $25,000 or less. They now use a blanket bond to cover those same officials at a cost of $1,026.[25]

Georgia law makes clear that blanket bonds must be in surety form with the official personally liable for claims against the bond. The Augusta-Richmond County director explained their blanket surety bond is in surety form with the official held liable for repayment of anything the surety company pays out on claims and that coverage remains the same as with the individual surety bond. According to the director, administering the blanket bond is much simpler than

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[23] See appendix E.
[24] Email from Don LeMond, November 22, 2013.
[25] Email from Sandy Wright, December 17, 2013.

the individual bond, and managing it takes less time. Coverage is limited to those acts that the official (1) personally benefits financially from the act complained of; or (2) was personally aware of and had actual knowledge of the act complained of; had actual knowledge that the act was illegal, contrary to law, or the breach of a duty imposed by law; and either acted to cause or failed to prevent the act complained of.[26]

Cobb County, Georgia, also buys a blanket surety bond. Their county risk management director said the county uses the blanket surety bond because it simplifies the process and saves the county time and money. He said that using individual bonds made compliance with the law difficult because of public official turnover and retirements. The blanket surety bond provides the same coverage—the "faithful discharge of duties" including the accounting for all money and property received by them by virtue of such position—as the individual surety bonds, and because coverage is tied to the position, not the person, coverage is automatic once the official takes office.[27] This blanket surety bond covers positions with separate bond amounts ranging from $1,000 to $150,000. Cobb County, Georgia's bond is shown in appendix G.

As demonstrated by Augusta-Richmond County and Cobb County, allowing local governments to use blanket surety bonds in place of multiple individual bonds could save local governments money while simplifying the process and providing the same coverage and safeguards. Appendix H gives an example of how this might be done in Tennessee.

Insurance as an Alternative to Surety Bonds

The use of other forms of risk management in place of individual public official surety bonds is not entirely novel. Other states have had alternative methods of risk management in place for years. The use of insurance to cover this risk, as proposed in Senate Bill 624, is allowed in six states. Appendix E includes a table listing other states' individual bond requirements for county governments along with any alternatives that are used or allowed. In addition to insurance, alternative methods include insurance pools and self-insurance.

Current Legislative Proposal

Senate Bill 624 would allow local governmental entities to purchase insurance instead of individual surety bonds or cover the same risk by participating in an insurance pool.[28] This bill was presented as a way to save local governments money, give them more flexibility, and reduce what some saw as too much governmental red tape. The bill allows for any one of three types of insurance coverage: (1) government crime coverage, (2) employee dishonesty insurance or (3) equivalent coverage that insures the faithful performance by officials and their employees of their fiduciary duties and responsibilities. A certificate of insurance would

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[26] Georgia Code, Section 45-4-24.
[27] Email from Brett LaFoy, December 16, 2013.
[28] This bill refers to pools established pursuant to Tennessee Code Annotated, Section 29-20-401.

"satisfy all requirements for the filing of the official bonds by the named officials." The bill sets minimum coverage at $400,000 per occurrence.

Comparison to Surety Bonds

Insurance policies that cover a group of officials would be easier to acquire than individual surety bonds for each official. The application process for surety bonds requires an investigation into the financial background of the official being bonded, typically with more investigation for larger bonds. The public official being bonded must complete a surety bond form at the statutorily defined dollar amount and file it with the appropriate office. An insurance policy covering a group of those officials would likely be easier to acquire because insurance companies do not typically investigate the individuals. With insurance, individuals are not investigated; the experience of the entire organization is considered instead. The insurance premium is based on that experience and the amount of coverage desired or required. Unlike individual surety bonds, insurance assumes losses will occur and is a mechanism to set money aside through premiums to cover them.

The actual cost of an insurance policy, as proposed by the bill, is currently unknown because a specific insurance policy was not provided to evaluate. While surety bonds are written in favor of the governmental entity, insurance is written in favor of the insurance company with many exclusions and exemptions. It is impossible to estimate costs based on types of policy coverage without knowing the exclusions and exemptions, as well as deductible amounts and other policy provisions. As written, the bill gives local governments great discretion in determining the contents of an insurance policy—such as deductible amounts, exclusions, and types of crimes covered—if they choose to use insurance instead of surety bonds. The result could be significant differences in coverage from county to county.

Moreover, the $400,000 minimum amount of coverage required by the bill is much lower than the amounts required for many public officials, which concerns state officials. For example, county trustees, especially those in more-populated counties, have surety bond coverage amounts in the millions of dollars. Other states have encountered this same issue when allowing insurance in place of official bonds.

And with less cost comes less coverage. The bill's fiscal note, while not giving a specific cost, does state that "insurance policies may ultimately be less expensive, but insurance comes with coverage limits and deductibles." The fiscal note on the bill indicated that insurance might increase tort liability, but "there should be a recurring decrease in local government expenditures because the cost associated with insurance policies are deemed less expensive than the cost associated with surety bonds."

The biggest concern with allowing the use of insurance in place of individual surety bonds is the difference in how they assign risk. With insurance coverage, risk is transferred from the individual and the official would no longer have any "skin in the game." In general, surety bonds make people individually accountable, while insurance does not. A surety bond will not be issued until the individual has been investigated, and the price of the bond will depend on

what the investigation reveals. In fact, the bonding company may refuse to issue a bond if they consider the risk too great. In other words, everything depends on the individual. Further, it is unclear whether an insurance policy can be written that provides the same coverage as Tennessee's public official surety bonds. Even if such policy could be written and found in the market place, it is widely believed that it would be prohibitively expensive. There are a number of other general differences between surety bonds and insurance policies. See table 2. For example, insurance policies are generally cancelable, while surety bonds may not be. The surety bond is issued for the term of office, whereas an insurance policy is typically on an annual term. The government as well as the public can file a claim against the official's surety bond. By contrast, under an insurance policy, unless third-party recoveries are specifically allowed by the policy, only the insured will be able to recover for a loss.

Table 2. Comparison of Insurance and Surety Bonds

Surety Bond	Insurance
Three party agreement. The surety guarantees the faithful performance of the principal to the obligee.	Generally, two party agreement. The insurance company agrees to pay the insured directly for certain losses incurred.
Losses not expected. The surety takes only those risks which its underwriting experience indicates is safe. A surety will usually look at the applicant's credit, arrest, and bankruptcy history, as well as any previous bond claims made against the applicant.	Losses expected. Insurance rates are adjusted to cover losses and expenses as the law of averages fluctuates.
Losses recoverable. After a claim is paid, the surety expects to recoup its losses from the principal. This means the public official has "skin in the game," and the risk of loss stays with the official.	Losses usually not recoverable. When an insurance company pays a claim, it usually doesn't expect to get repaid by the insured. Risk of loss is transferred to the insurance company.
The cost of the bond covers expenses. A large portion of the surety bond price is really a service charge for weeding out unqualified candidates and for issuing the bond.	Premium covers losses and expenses. Insurance premiums are collected to pay for expected losses.
Sureties are selective.	Insurers cover most risks. The insurance agent generally tries to write a policy on anything that comes along (at the appropriate premium rate) and allows for a large volume to cover the risk.
2 or 3 page document.	Often a multipage document containing many exclusions and exemptions.

Surety Bond	Insurance
Written in favor of the state. Statute requires that the bond form be "prescribed by the Comptroller of the Treasury, with the approval of the Attorney General and Reporter."[29]	Typically, written in favor of the insurance company.
Amount of Coverage: Bond amounts vary from $2,000 to well over $10 million depending on the applicable statutory requirements for the position. For some officials, this is a specific amount as stated in the law. For other officials, the amount is based on the amount of local revenues or on population. And for some, the amount of the bond is determined by the legislative body or presiding judge.	Amount of Coverage: Senate Bill 624 proposes that "any such policy shall have limits of not less than $400,000 per occurrence."
Tennessee's official bonds allow any injured party to recover on the bond. Part (3) of 8-19-301 states that official bonds under this code are "for the use and benefit of every person who is injured, as well as by any wrongful act committed under color of such officer's office as by the failure to perform, or the improper or neglectful performance, of the duties imposed by law." Official bonds are not issued for the protection of the official himself, but rather to protect the government or the public from any injuries caused by the public official while in office.	Third party may not bring suit. Policy usually written to only allow recovery for the insured. That is, the policy is written for the sole benefit of the insured, the governmental entity.

[29] Tennessee Code Annotated, Section 8-19-101(b)(1).

Surety Bond	Insurance
Coverage: The statutes contain two basic obligations: (1) that the official faithfully discharge or perform the duties of the office; and (2) that the official truly account for and turn over public money, property, and records entrusted to the official by the duties of office. The public official bond covers the failure of the bonded official to carry out either one of these duties with the motives of the official being irrelevant. A breach of the bond can occur as the result of the failure to act, negligence of the principal, or intentional conduct, i.e., nonfeasance, misfeasance, and malfeasance. In essence, the failure to faithfully discharge one's duties may be attributed to either failing to take a required act or failing to refrain from doing something which by its nature should not have been done. Provided that loss occurs to one entitled to recover on a bond, all liability on a public official bond is absolute and is predicated on breach of duty.	Coverage: In theory, insurance could cover everything that the bond covers. Senate Bill 624 proposes allowing the optional use of a policy of insurance or an agreement with an administrative agency or pool established pursuant to Tennessee Code Annotated, Section 29-20-401, that provides government crime coverage, employee dishonesty insurance coverage, or equivalent coverage that insures the faithful performance by officials and their employees of their fiduciary duties and responsibilities.

Source: CNA Surety. 2012. "Suretyship: A Practical Guide to Surety Bonding," http://www.thebondexchange.net/Applications/Suretyship.pdf (accessed January 17, 2014).

Crime or Dishonesty Insurance

The first two options offered by the bill are similar. Crime insurance, commonly referred to as fidelity insurance, typically protects organizations from loss of money, securities, or inventory resulting from crime. Claims often allege employee dishonesty, embezzlement, forgery, robbery, safe burglary, computer fraud, wire transfer fraud, counterfeiting, and other criminal acts. Employee dishonesty insurance typically covers theft of money, securities, or property, and is usually written with a per loss limit, a per employee limit, or a per position limit. Obviously, there is considerable overlap in what these two types of insurance cover, and the phrases are sometimes used interchangeably. Individuals cannot insure themselves against their own intentional unlawful acts. Consequently, with a crime or dishonesty policy, the governmental entity would be the insured and not the official.

The cost of crime or dishonesty insurance would likely be less than that of a bond; however, the coverage would also be less. For example, the typical crime- or dishonesty-type policy would not provide coverage for negligence or faithful performance of duties unless specific endorsements for those types of coverage were added to the policy, which could increase the

price. Even if those endorsements were included, there would be exemptions and exclusions, thus limiting overall coverage.

Six states allow some form of crime insurance to be used in place of an official bond requirement. Four of the states—California, Colorado, Idaho, and Indiana—specifically require crime insurance to be used. Indiana requires that the crime insurance include an endorsement for "faithful performance." Pennsylvania allows "crime-fidelity" insurance endorsed for "faithful performance" to be used in place of the individual bond. Utah allows a "fidelity bond or theft and crime insurance" to be used in instead of the individual bond requirements.

Insurance Equivalent to Surety Bond Coverage

The third option offered by the bill, "equivalent coverage that insures the faithful performance by officials and their employees of their fiduciary duties and responsibilities," would appear to make insurance equivalent to surety bonds. It does not, because the public official is not made accountable by it. In order to recover losses by the public official, the insurance carrier or the governmental entity would have to press charges or take him to court. That issue aside, to provide equal coverage, multiple endorsements for various types of coverage would have to be included in the policy and, like a surety bond, it would have to have no deductible.

Since this specific type of insurance coverage has not been used in Tennessee, at best, only an estimate could be made on the cost of initial premiums. Insurance agents and state officials interviewed have indicated that the initial premiums could be high because there is no market experience in Tennessee with this particular type of insurance product and that, even if such a policy could be written and found in the marketplace, it would probably be prohibitively expensive.

Insurance Pools

Senate Bill 624 would also allow the insurance to be provided through an insurance pool established pursuant to Tennessee Code Annotated, Section 29-20-401. This section of the code was created to allow governmental entities to enter into "pooling" agreements to manage their liability exposure under the Tennessee Governmental Tort Liability Act. Pooling agreements allow the member entities to transfer their exposure for financial losses to the group as a whole in return for payments to the pool.[30] In effect, they are privately held insurance companies, owned by the members, and not regulated by the state. The services related to the transfer of that risk are provided by the new entity, the pool, or by third parties (underwriters, excess carriers, etc.) retained by the pool.[31] The governmental entity and taxpayers become liable for any losses not covered by the pool, and the public official no longer has any "skin in the game."

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[30] Doucette 2001.
[31] Ibid.

Pools are created and regulated differently from state-to-state, with some states regulating pools like insurance.[32] State insurance regulation typically has four objectives: (1) ensuring that consumers are charged fair and reasonable prices for insurance products; (2) protecting the solvency of insurers; (3) preventing unfair practices and overreaching by insurers; and (4) guaranteeing the availability of coverage to the public.[33] Using pools to provide coverage creates additional risks. The members of a pool have joint and several liability, meaning responsibility for each other's claims in proportion to the payments made to the pool or as the pooling agreement states.

Pools are allowed to provide coverage in place of surety bonds for officials in six states. Arkansas established a state-run, statewide pool that provides coverage for all state and local officials in place of the previously required surety bonds. Their pool covers only losses up to $250,000 caused by fraudulent or dishonest acts, and not the faithful performance of duties. North Dakota's State Bonding Fund operates as a pool to provide coverage for public officials. Idaho allows counties and cities to provide coverage through an insurance pool instead of using individual surety bonds. The Idaho County Risk Management Program is a member-owned local-government insurance pool that includes endorsements for faithful performance, which is broader than Arkansas's coverage. Georgia, Maine, and New Jersey all allow different types of insurance pools to provide coverage as a substitute for official bonds.

Self-insurance—an Option Offered in Other States

Self-insurance, setting aside funds to cover potential future losses, is another risk management tool—while not specifically mentioned in the bill—that is used in other states. Four states allow self-insurance as a substitute for individual bonds for county officials. California, Illinois, Louisiana, and Texas allow local governments to use self-insurance in place of surety bonds.

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[32] Ibid.
[33] Jerry 2001.

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Persons Interviewed

Phil Adams, Analyst
Tennessee Department of Commerce and Insurance

Jim Arnette, Director
Division of Local Government Audit
Tennessee Comptroller of the Treasury

Ashley Arnold, General Counsel
Insurors of Tennessee

Charles Bidek, Chief Executive Officer
Insurors of Tennessee

Mark Bowery, County Commissioner
Sullivan County, Tennessee

Drew Carpenter, Director
Risk Management Division
Arkansas Insurance Department

Kit Coffin, Risk Management Program Manager
Idaho Department of Administration

David Connor, Executive Director
Tennessee County Commissioners Association

Jim Cope, County Attorney
Rutherford County, Tennessee

Leah May Dennen, Sumner County Law Director
Sumner County, Tennessee

John Duncan, Manager
Property and Casualty Unit
Tennessee Department of Commerce and Insurance

John Evans, President
NGU Risk Management

Wayne Franklin, Risk Manager
Williamson County, Tennessee

Nathan Green, Lobbyist
RobinsonGreen, LLC

Brent Greer, County Mayor
Henry County, Tennessee
Commissioner, TACIR

Sarah Hiestand, Senior Counsel
Financial Division
Office of the Tennessee Attorney General and Reporter

Brian Hoffmeister, Director of Policy Analysis
Tennessee Department of Commerce and Insurance

Pat Hollingsworth, County Finance Officer
Henry County, Tennessee

Ann Holthoff, Risk Consultant
Risk Management Division
Arkansas Insurance Department

Josh Jones, Legal Consultant
University of Tennessee, Municipal Technical Advisory Service

Durema Kissam, Senior Commercial Surety Specialist
The Hartford

Robert T. (Bobby) Lee, General Counsel
Tennessee Comptroller of the Treasury

Brett LaFoy, Risk Management Director,
Cobb County, Georgia

Don LeMond, Director of Risk Management
Virginia Department of the Treasury

Jerry Mason, General Counsel
Idaho Counties Risk Management Program

Libby McCroskey, Senior Legal Consultant
University of Tennessee, County Technical Assistance Service

Rachel Newton, Assistant General Counsel
Tennessee Comptroller of the Treasury

Lea Niebuhr, Senior Claims Examiner
RLI Corporation

Richard Norment, Assistant to the Comptroller for the Department of Audit
Tennessee Comptroller of the Treasury

Mark Norris, State Senator
District 32, Tennessee
Chairman, TACIR

Mark Shambaugh, Branch Manager
RLI Corporation

Jack Spann
Spann Insurance

Melissa Stinson, Risk Management Director
Rutherford County, Tennessee

Curry Todd, State Representative
District 95, Tennessee

Joyce Welborn, Legislative Auditor
Tennessee Comptroller of the Treasury

Craig Wild, Clerk and Master
Cocke County, Tennessee

Greg Worley, Audit Review Manager
Tennessee Comptroller of the Treasury

Bob Wormsley, President/Chief Executive Officer
Local Government Insurance Pool

Sandy Wright, Risk Management Director,
Augusta-Richmond County, Georgia.